

CALIFORNIA
STATE
SENATE



SENATOR BILL MORROW

CAPITOL OFFICE
ROOM 4048
(916) 445-3731

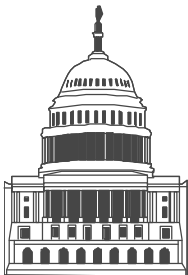
ORANGE COUNTY OFFICE
(949) 489-9838

SAN DIEGO COUNTY OFFICE
(760) 434-7930

WWW.SEN.CA.GOV/MORROW

WADE C. TEASDALE
CHIEF OF STAFF

CAROLE MARKS
DISTRICT COORDINATOR



MAY 31, 2002

Senator Bill Morrow

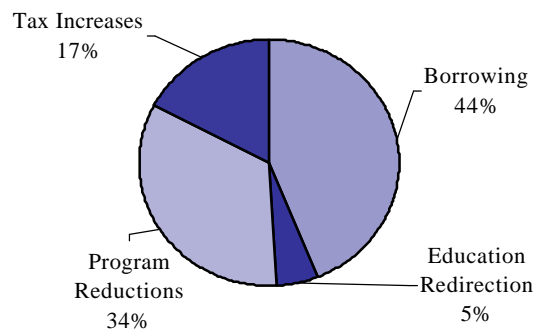


Capitol Update

GOVERNOR'S REVISED BUDGET BUSTS THE BANK: RAISING TAXES

Governor Davis released the annual "May Revision" to his proposed 2002 budget. The May Revision provides an update to his spending plan released in early January. The changes reflect the most recent estimates of economic indicators and budgetary forecasts. Despite the estimated shortfall of \$23.6 billion, the budget still spends \$98.9 billion.

GOVERNOR'S PROPOSAL TO CLOSE THE \$23.6 BILLION GAP



Tax Increases At The Heart Of the May Revision

This budget is based on a \$1.2 billion sales tax increase, which became effective on January 1, 2002. Davis' January budget included an additional \$240 million in tax increases. Governor Davis' May Revision proposes close to \$4 billion in tax increases, which includes:

- A 131 percent increase in the annual car tax which will cost Californians \$1.3 billion 2002-03; \$1.1 billion 2003-04. **Tax increase: \$2.4 billion.**
- A two-year suspension of the net operating loss (NOL) tax credit, costing California companies \$800 million 2002-03; \$350 million gain 2003-04.
Total Tax Increase: \$1.2 billion or \$2.4 billion over the next two years.
- The imposition of an additional 50-cent per pack cigarette/tobacco tax, increasing the per-pack tax from 87-cents to \$1.37 per pack, an annual **tax increase of \$475 million**

RURAL COMMUNITIES

The Governor's May Revision includes the following significant cuts to rural and agricultural communities:

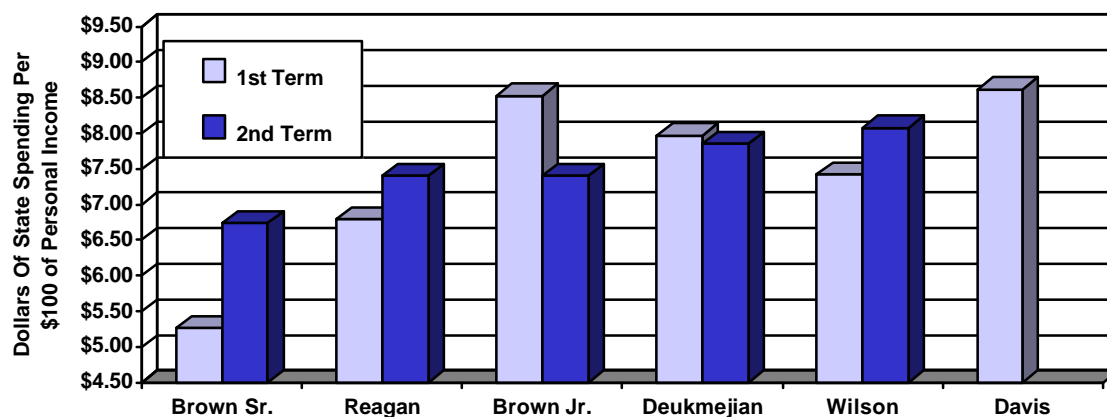
- ◆ "Buy California," the agriculture promotion program, is proposed to be cut by \$3 million.
- ◆ The Rural Economic Development Infrastructure Revenue Bond Fund is proposed to be cut by \$8.4 million.
- ◆ The Bio-mass to Energy Grant Program is proposed to be reduced by \$2 million.
- ◆ The Pierce's Disease Management and Control is proposed to be reduced by \$1.57 million.
- ◆ The \$8.5 million included in the January budget for the Farmworker Housing Program is eliminated from the General Fund budget and is instead proposed to be funded only if a multi-billion dollar general obligation bond is passed by the voters in November 2002.
- ◆ The "War on Methamphetamine" program is proposed by the Governor to be cut by \$5 million, resulting in a one-third reduction in program funds.

EXPENSIVE AND RISKY PROPOSAL TO SOLVE THE SHORTFALL

Securitize Tobacco Settlement Funds – Each year, the state receives \$400 million from the tobacco settlement. In January, the Governor proposed to engage in leverage financing with half of the revenues California will receive over the next 22 years. The Governor's budget in January proposed borrowing \$2.4 billion, based on the expected revenue stream over the next 22 years, costing \$4.2 billion in principal and interest costs. The May Revision instead proposes to use almost all of the annual Tobacco Tax Settlement each year by issuing \$4.5 billion in bonds, which will cost California well over \$10 billion. **This means that, in 2020, Californians will still be paying for this year's operating expenses of the state government.**

Additionally, the Governor announced that in his revised budget he proposes to borrow and loan an unprecedented \$10 billion. The multiple borrow schemes contrived in this budget will cost the state billions of dollars in future budget years, potentially creating annual deficits for years to come.

Historical State Spending On A Population And Inflation Adjusted Basis



STATE WORKER BENEFITS

Despite the significant deficit the state is facing, the May Revision includes over \$196 million in pay and benefit increases for public employees:

Employee Pay Raises	\$54.5 million
Health and Dental Benefits for Annuitants	\$23 million
Public Retirement Employees' Retirement System (CalPERS)	\$75.9 million
State Teachers' Retirement System (STRS)	\$42.7 million
TOTAL	\$196 million

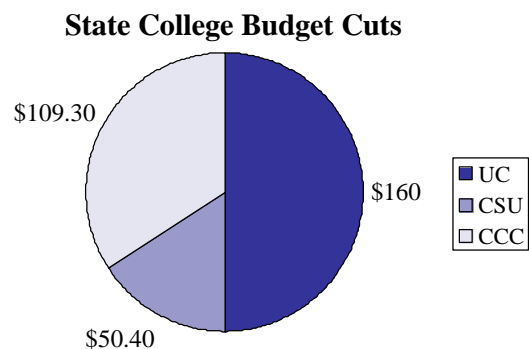
K-12 EDUCATION

The Governor's proposed May Revision:

- ◆ Funds the minimum required by law (Proposition 98). This will result in an increase of approximately \$1.2 billion. Of this amount, \$848 million is from the General Fund and \$335 million from an increase in local property taxes allocated to education.
- ◆ Reduces funds for K-12 Education by \$1.2 billion over two years in General Fund monies.
- ◆ Does not fund special education cost of living adjustment (COLA) and growth with state Prop. 98 funds. Instead, the over \$110 million in new federal special education dollars will be used to fund COLA and growth.
- ◆ Includes a 10% reduction in all K-12 Independent Study funding.
- ◆ Reduces funds for instructional materials by \$145 million with science equipment taking the biggest cut of \$75 million.
- ◆ Preserves \$29.7 million for the expansion of Before and After School Program grants that were suspended in the current year and \$45.3 million for additional expansion to provide services to at least 79,000 additional school-age children.

HIGHER EDUCATION

State colleges also feel the pinch of Governor Davis' overspending. While University of California schools take the biggest hit with a \$160 million reduction, Community Colleges take the second largest hit with a \$109.3 million reduction. The California State University also feels the cuts with a \$50.4 million reduction.



STUDENT AID COMMISSION

- ◆ Eliminates the California Work Study Program (\$5.3 million cut).
- ◆ At a time when the state is in critical need of qualified teachers the Governor reduces the number of Cal Grant vocational and teachers' education programs, which benefit those seeking teaching certificates and vocational careers. The reduction will be \$7 million.

LOCAL GOVERNMENT

The May Revision includes over \$1 billion in budget cuts to local governments, including:

- ◆ \$39 million – Elimination of Williamson Act Subventions.
- ◆ \$120 million – ERAF increased payments by mandating that multi-county special districts and community development agencies pay into the ERAF fund. Multi-county special districts would pay approximately \$45 million into the ERAF while community redevelopment agencies would pay \$75 million.
- ◆ \$38 million – Eliminate booking fees to cities and special districts for reimbursements paid to counties and other cities.
- ◆ \$111 million – Eliminate grants to counties for Juvenile Justice Crime Program.
- ◆ \$16.9 million – Reduction of technology grants to local law enforcement program.
- ◆ \$19.4 million – Eliminates half of the funds provided for local law enforcement grants through the Office of Criminal Justice Planning.
- ◆ \$45 million – Delayed Child Support Data System.
- ◆ \$238 million – County Health and Welfare Administration.
- ◆ \$35 million – 10% County Share of Cost for EPSDT.
- ◆ \$168 million – Suspend State Mandate Payments.

TRANSPORTATION

- ◆ The Governor's May Revision diverts another \$373 million from the Traffic Congestion Relief Fund (TCRF) and another \$50 million from the State Highway Account (SHA) to help balance the General Fund deficit. This is addition to the \$672 million raid on the TCRF and \$474 million from the SHA proposed by the Governor in January.
- ◆ The May Revision includes a reduction of \$17.3 million for Special Transportation Programs. These reductions result in a revised funding level of \$98 million.

HEALTH CARE

The Governor proposes to further reduce the amount the State reimburses physicians, dentists and other health care providers who treat Medi-Cal recipients by partially rescinding the modest increases provided in 2000. The Governor proposed \$155 million in provider reimbursement cuts in January and now proposes an additional cut of \$94 million to health care providers. Even prior to the Governor's proposed cuts, current rates for physician payments average 50-60 percent of Medicare rates and are far below rates for private pay patients. In more affluent areas, the lower rates are more readily absorbed. This is a critical problem in the Central Valley, where a disproportionate share of Medi-Cal recipients reside. This is especially relevant in that low Medi-Cal reimbursement rates make it impossible to attract and retain health care professionals.

WELFARE BENEFIT INCREASES

The Governor proposes to increase by \$92.2 million the California Food Assistance Program, which provides food stamps to persons who are not eligible for federal Food Stamps because of their immigration status.

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